

Department of Health and Human Services
DEPARTMENTAL APPEALS BOARD
Appellate Division

Maryland Disability Law Center
Docket No. A-15-110
Decision No. 2843
January 5, 2018

DECISION

The Maryland Disability Law Center (MDLC), a nonprofit organization, receives annual grants awarded by the Substance Abuse and Mental Health Services Administration (SAMHSA) under the Protection and Advocacy for Individuals with Mental Illness (PAIMI) program. Those grants enable MDLC to carry out its role as the State of Maryland's designated Protection & Advocacy (P&A) agency, responsible for advocating for and protecting the civil rights of persons with mental illness.

At issue in this appeal is SAMHSA's August 7, 2015 determination to disallow \$12,657 of costs charged by MDLC to its PAIMI grants for fiscal years (FYs) 2008 through 2011. (For grant accounting purposes, MDLC's fiscal year is October 1 through September 30.) MDLC contends that the "vast majority" of the disallowed costs are adequately documented and "clearly allowable" charges to its PAIMI grants. We conclude, however, that MDLC has substantiated the allowability of \$2,584.13 of the disputed costs. Accordingly, we reduce the disallowance by that amount and affirm the balance of the disallowance, which totals \$10,072.87 (or \$12,657 minus \$2,584.13). We also deny MDLC's request that the disallowance be set aside on the ground it amounts to a "vindictive" or "arbitrary" action by SAMHSA.

I. Legal Background

A. The PAIMI program

The federal Protection and Advocacy for Individuals with Mental Illness Act of 1986, 42 U.S.C. § 10801 et seq., authorizes annual federal grants to organizations (such as MDLC) that states have designated as protection-and-advocacy "systems" with authority and responsibility to protect and advocate for the rights of individuals with mental illness. *See* 42 U.S.C. §§ 10801(a)(1), (b)(1), (b)(2), 10803, 10805(a)(1). SAMHSA administers the PAIMI grant program under regulations published in 42 C.F.R. Part 51. In general, PAIMI program grants "are to be used to pursue administrative, legal, and other appropriate remedies to redress complaints of abuse, neglect, and rights violations and to protect and advocate for the rights of individuals with mental illness through activities to

ensure the enforcement of the Constitution, and Federal and State statutes.” *Substance Abuse and Mental Health Services Administration; Requirements Applicable to Protection and Advocacy of Individuals with Mental Illness; Final Rule*, 62 Fed. Reg. 53,548, 53,549 (Oct. 15, 1997); *see also* 42 U.S.C. §§ 10801(b), 10805(a); 42 C.F.R. §§ 51.6(f), 51.7(b).

Each state’s protection-and-advocacy system must have a “governing authority responsible for its planning, designing, implementing and functioning,” including the setting of annual “[p]rogram priorities and policies.” 42 C.F.R. §§ 51.22(a), 51.24(a). In addition, a protection-and-advocacy system must establish an “advisory council” that is charged with, among other responsibilities, “[p]rovid[ing] independent advice and recommendations to the [protection-and-advocacy] system” and “[w]ork[ing] with the [system’s] governing authority in the development of policies and priorities.” *Id.* § 51.23(a). The PAIMI program regulations provide that the advisory council “shall meet no less than three times annually.” *Id.* § 51.23(b)(3). “At least 60 percent of the membership of the advisory council shall be comprised of individuals who have received or are receiving mental health services or who are family members of such individuals.” *Id.* § 51.23(b)(1).

B. Grant administration and cost principles applicable to PAIMI grants

PAIMI grants and other awards issued by constituent agencies of the Department of Health and Human Services (HHS) are subject to the uniform grant administration regulations published in title 45 of the Code of Federal Regulations. *See* 45 C.F.R. § 51.4. When MDLC charged its PAIMI grants for the disallowed costs, HHS’s uniform grant administration regulations, as applicable to nonprofit organizations (such as MDLC), were found in Part 74 of that title. *Id.* (Oct. 1, 2011); 45 C.F.R. Part 74 (Oct. 1, 2011). (Although the Part 74 regulations have since been superseded, we apply them here because they were in effect during the fiscal years when the disallowed costs were incurred and charged to MDLC’s PAIMI grants. *Teaching & Mentoring Communities, Inc.*, DAB No. 2790, at 7 n.6 (2017).)

HHS’s grant administration regulations state that the “allowability of costs incurred” by a nonprofit organization – that is, the degree to which those costs may be reimbursed under a federal grant or other “award” – is determined in accordance with federal “cost principles” set forth in Office of Management and Budget (OMB) Circular A-122.¹ 45 C.F.R. § 74.27(a) (Oct. 1, 2011). During the fiscal years relevant to this dispute, the content of OMB Circular A-122 was codified in 2 C.F.R. Part 230 (Jan. 1, 2012).

¹ In late 2014, the Part 74 regulations and OMB Circular A-122 were superseded by the Uniform Administrative Requirements, Cost Principles, and Audit Requirements for HHS Awards published in 45 C.F.R. Part 75. *See* 79 Fed. Reg. 75,872, 75,875-76 (Dec. 19, 2014).

In order for a cost to be allowable under federal cost principles, it must meet the following requirements (among others): (1) “[b]e *reasonable* for the performance of the award”; (2) be “*allocable to*” the award; and (3) “[b]e *adequately documented*.” 2 C.F.R. Part 230, App. A, ¶ A.2 (Jan. 1, 2012) (italics added).

In general, a cost is “reasonable” within the meaning of the cost principles “if, in its nature or amount, it does not exceed that which would be incurred by a prudent person under the circumstances prevailing at the time the decision was made to incur the costs. . . .” *Id.*, App. A, ¶ A.3 (Jan. 1, 2012). In judging the reasonableness of a cost, “consideration shall be given to,” among other factors, “[w]hether the cost is of a type generally recognized as ordinary and necessary for the operation of the organization or the performance of the award.” *Id.*, App. A, ¶ A.3.a (Jan. 1, 2012).

A cost is “allocable to” an award “in accordance with the relative benefits received.” *Id.*, App. A, ¶ A.4.a (Jan. 1, 2012). In other words, if a cost incurred by the grantee confers a “benefit” on more than one “cost objective” – such as a grant program or other source of funding for the grantee – “then the cost must be allocated among those [cost] objectives in proportion to the benefit that each . . . receives as a result of the cost having been incurred.” *Child Care Assoc.*, DAB No. 2739, at 3 (2016). Overall, the cost principles “are designed to provide that the Federal Government bear its fair share of costs except where restricted or prohibited by law.” 2 C.F.R. § 230.15 (Jan. 1, 2012); *see also Univ. of Ca.*, DAB No. 2662, at 3 (2015).

A grantee must be able to document the existence and allowability of costs charged to a federal award. *New City Health Ctr.*, DAB No. 1686, at 10 (1999); *see also Tenn. Protection & Advocacy, Inc.*, DAB No. 1454, at 4 (1993) (“It is the responsibility of the grantee to have in place adequate internal controls to maintain the records necessary to document its use of federal funds.”). The Board has consistently characterized this obligation as “fundamental.” *New City Health Ctr.* at 10; *Central Piedmont Action Council, Inc.*, DAB No. 1916, at 13 (2004).

C. The awarding agency’s disallowance authority

If a grantee “materially fails to comply with” a grant’s “terms and conditions” – “whether stated in a Federal statute or regulation, an assurance, an application, or a notice of award” – then the HHS awarding agency may “[d]isallow (that is, deny both use of funds and any applicable matching credit for) all or part of the cost of the activity or action not in compliance.” 45 C.F.R. § 74.62(a)(2) (Oct. 1, 2011). In this case, the PAIMI grants’ “terms and conditions” include the uniform grant administration regulations in 45 C.F.R. Part 74, the cost principles made applicable by those regulations, and the statute and regulations which govern the PAIMI program. *See* 42 C.F.R. § 51.4 (stating that HHS’s

uniform grant administration requirements and cost principles “apply to grants funded under” the PAIMI program); SAMHSA Ex. B (award notices indicating that the terms and conditions of MDLC’s PAIMI grants include the PAIMI program statute and regulations and HHS’s grant administration regulations); *North Valley Cmty. Health Assn.*, DAB No. 509, at 5-6 (1984) (stating that an award’s terms and conditions include statutes and regulations incorporated by reference in the award notice).

II. Case Background

During January 2012, SAMHSA performed an on-site audit (what it called a “fiscal site visit review”) of MDLC to verify that it was complying with the terms and conditions of its PAIMI grants. *See* SAMHSA Ex. C; SAMHSA Ex. J at 2. As a result of that on-site audit, SAMHSA questioned \$25,614 in costs that MDLC had charged to its PAIMI grants for FYs 2008-2011 and asked MDLC for documentation of the costs’ allowability.² SAMHSA Ex. D. During March 2012, MDLC sent SAMHSA documentation and a letter contending that most of the questioned costs were allowable. *See* SAMHSA Exs. E, F, and G.

On April 4, 2014, SAMHSA sent MDLC a letter stating the “results” of its 2012 audit. SAMHSA Ex. H. The letter states that MDLC had been “unable to demonstrate that \$23,144 . . . charged to [MDLC’s] PAIMI grants [were] allowable . . . in accordance with federal requirements.”³ *Id.* That figure (\$23,144) reflected costs incurred by MDLC for membership dues, advisory council stipends, travel, professional services, equipment rental, and other items or services. *Id.*

On August 15, 2014, MDLC sent a check to SAMHSA for some of the questioned costs identified in the April 4, 2014 letter. *See* SAMHSA Ex. I (Aug. 15, 2014 letter at 12). For other questioned costs, MDLC provided additional documentation and explanation. *Id.* (miscellaneous attachments to Aug. 15, 2014 letter).

On August 7, 2015, SAMHSA issued a formal notice of disallowance, requesting that MDLC “return \$12,657 in unallowable costs” identified on an attached spreadsheet. The spreadsheet is SAMHSA Exhibit A. For each disallowed cost, the spreadsheet specifies documentation supplied by MDLC during the audit process and SAMHSA’s basis for finding the cost unallowable. The disallowed costs include:

² The PAIMI grants implicated by the disallowance are identified, by grant number and project period, in SAMHSA Exhibits B and H.

³ SAMHSA’s April 4, 2014 letter also directed MDLC to remedy certain allegedly deficient personnel, accounting, and financial management practices – none of which is at issue here.

- Membership fees paid to the National Disability Rights Network (\$410.48)
- Water cooler rental (\$268.75)
- Coffee services (\$518.78)
- Audit and accounting (\$1,493.09)
- Office moving (\$896.69)
- Video camera (\$55.97)
- Miscellaneous “supermarket” items (\$113.74)
- Printing (\$477.63)
- Cleaning services performed by employee (\$18.55)
- Professional services (\$4,027.44)
- Travel (\$2,392.63)
- Employee bonuses (\$583.30)
- PAIMI advisory council stipends (\$1,400)

III. Discussion

In an appeal challenging the disallowance of costs charged to a federal award, the HHS awarding agency has the initial burden to provide sufficient information about the basis for the disallowance to enable the grantee to respond. *Me. Dep’t of Health & Human Servs.*, DAB No. 2292, at 9 (2009), *aff’d*, *Me. Dep’t of Human Servs. v. U.S. Dep’t of Health & Human Servs.*, 766 F. Supp. 2d 288 (D. Me. 2011). If the agency carries that “minimal” burden – and there is no claim that SAMHSA has failed to do so here – then the grantee must demonstrate, with appropriate documentation, that disputed costs charged to the award were actually incurred and allowable under the award’s terms and conditions. *Mass. Exec. Office of Health & Human Servs.*, DAB No. 2218, at 11 (2008), *aff’d*, *Mass. v. Sebelius*, 701 F. Supp.2d 182 (D. Mass. 2010); *Child Care Assoc.* at 6; *Dr. Arenia C. Mallory Cmty. Health Ctr., Inc.*, DAB No. 2659, at 6-7 (2015). That burden entails demonstrating that any cost which benefits more than one program, funding source, or other cost objective has been allocated to the relevant grant on an equitable basis – that is to say, “in accordance with the relative benefits received” by each cost objective. *Vt. Slauson Econ. Dev. Corp.*, DAB No. 1955, at 2-3 (2004).

We now discuss, in subsection A, whether MDLC has substantiated the allowability of each category or group of disputed costs. In subsection B, we address certain overarching objections by MDLC to SAMHSA's disallowance determination.

A. Allowability of disputed costs

1. *Membership fees paid to the National Disability Rights Network* (\$410.48)

MDLC – which receives funding from various federal and nonfederal sources in addition to the PAIMI program – pays annual membership fees to the National Disability Rights Network (NDRN). *See* SAMHSA Ex. A (item 153); MDLC Ex. AA (item 153); MDLC Ex. CC at 17, 21-22. In November 2008, MDLC paid NDRN membership fees totaling \$5,600, of which it allocated \$410.48 (or 7.3 percent) to its PAIMI grant. MDLC Ex. AA (item 153). SAMHSA disallowed that allocated amount on the ground that MDLC had failed to provide “documentation (spreadsheet with allocation of costs) to support the federal allotment and the percentage of the costs charged to the PAIMI grant[.]” SAMHSA Ex. A (item 153 (“OFAS Comments”)).

As noted, under federal cost principles, a nonprofit grantee's costs are allowable, or eligible for federal reimbursement, under a federal award only to the extent they are “allocable to” that award. While recognizing that NDRN membership fees are potentially reimbursable under a PAIMI grant, *see* SAMHSA Ex. A (item 153 (“OFAS Comments”)), SAMHSA was unable to verify that \$410.48 represented the PAIMI program's allocable share – that is, the program's share as determined in accordance with “relative benefits received” – of total NDRN membership fees paid by MDLC in November 2008. Consequently, MDLC had the burden in this proceeding to demonstrate that the fees disallowed were allocable to its PAIMI grant for the relevant fiscal year (presumably FY 2009). *Child Care Assoc.* at 6, 9. To carry that burden, MDLC needed to produce accounting records and policies, or other contemporaneous business records, showing how it calculated the PAIMI program's share of the fees and the reasonableness of the allocation method. *Id.* at 9; *see also Ohio Dep't of Public Welfare*, DAB No. 453, at 8-9 (1983) (holding that “source documentation” was needed to substantiate an allocation of costs to a particular cost objective “to the extent of benefits received”); *Recovery Consultants of Atlanta, Inc.*, DAB No. 2305, at 5-6 (2010) (upholding a disallowance when grantee failed to produce “evidence or explanation” showing that allocation percentages “were calculated using appropriate distribution bases determined using current data, as required”); *Tenn. Protection and Advocacy, Inc.* at 4-5 (upholding a disallowance of costs unsupported by “contemporaneous” records); *Nat. Alliance on Mental Illness*, DAB No. 2612, at 7 (2014) (stating that the Board “generally will not rely on non-contemporaneous documentation as evidence to support claimed costs” and that such documentation “must be closely scrutinized”).

MDLC has not carried that burden. Although it apparently gave SAMHSA proof (an invoice and cancelled check) that it paid \$5,600 for NDRN membership fees in November 2008,⁴ *see* MDLC Ex. A (item 153), MDLC has produced no accounting or other records showing the method used and calculations made to allocate the fees – or any other disallowed costs – among its various funding sources or other cost objectives.

MDLC asserts that it “clearly explained its allocation methodology in detail” in an August 15, 2014 letter to SAMHSA. Appellant’s Brief (App. Br.) at 6. That letter describes what MDLC claims to have been its “methodology” for allocating “indirect costs” incurred during FYs 2008, 2009, and 2010. SAMHSA Ex. I (Aug. 15, 2014 letter at 10-13). According to the letter, MDLC allocated indirect costs for those three fiscal years by applying a ratio (recalculated quarterly) of “direct hours for the funding source” to “total direct hours.” *Id.* (Aug. 15, 2014 letter at 11). That after-the-fact explanation has little value or meaning in the absence of records verifying that MDLC treated NDRN membership fees as indirect costs and actually applied the described methodology to compute the PAIMI program’s share of NDRN membership fees. The need for contemporaneous records is underscored by MDLC’s admission in the August 15, 2014 letter that accounting policies and procedures “were not always followed by . . . staff to ensure that all costs charged to its federal grants were reasonable, allocable, and adequately documented.” *Id.* (Aug. 15, 2014 letter at 8). Furthermore, the letter’s description of MDLC’s pre-2011 indirect cost methodology is far from complete or comprehensible, failing to explain how or why it should be thought to have allocated indirect costs in accordance with “relative benefits received.” On the topic of whether indirect costs were allocated equitably, the August 15, 2014 letter merely states that MDLC’s allocations met some undefined standard of “reasonableness.” *See id.* (Aug. 15, 2014 letter at 12 (stating that “if [indirect] expenditures charged to PAIMI were approximately 14%, [then] the percentage allocated is deemed to be reasonable”)).

MDLC submitted an “Accounting Policies and Procedures Manual” (MDLC Ex. CC), asserting that this document “sets forth additional relevant detail.” App. Br. at 6. But the manual has a “revised” date of August 2014, and we see nothing in that document which purports to describe MDLC’s cost allocation practices during 2008, when MDLC incurred the membership fees at issue here.

MDLC asserts that it has “access to” relevant cost accounting data but that because “SAMHSA sat on this audit for months and years at a time,” it no longer uses the accounting or other software that houses or manipulates that data and no longer employs persons capable of preparing or interpreting the necessary cost “reports.” *See* Appellant’s Reply Brief (Reply) at 7-8; SAMHSA Ex. I (Aug. 15, 2014 letter at 10, 11-12). MDLC

⁴ MDLC did not submit copies of those documents for the appeal record.

further suggests that it would be too expensive to hire someone with the necessary expertise to perform those tasks. Reply at 8; SAMHSA Ex. I (Aug. 15, 2014 letter at 11). These allegations are unsubstantiated, but even if they are true, they do not excuse MDLC's failure to produce adequate documentation. As a federal award recipient, MDLC is responsible for creating and maintaining accounting, record-keeping, and other systems capable of documenting the allowability of costs questioned by the HHS awarding agency. *See generally* 45 C.F.R. § 74.21(b)(2), (6), and (7) (requiring that a grantee's "financial management systems" implement or provide "[r]ecords that identify adequately the source and application of funds for HHS-sponsored activities"; "[w]ritten procedures for determining the reasonableness, allocability and allowability of costs in accordance with the provisions of the applicable Federal cost principles and the terms and conditions of the award"; and "[a]ccounting records, including cost accounting records, that are supported by source documentation"); *Nat. Alliance on Mental Illness* at 6 (explaining a grantee's responsibility to ensure that it, and any "subrecipient" of federal award funds, have systems in place to generate and maintain the records necessary to substantiate the allowability of costs charged to federal awards); *N.Y. State Dep't of Social Servs.*, DAB No. 1076, at 24 (1989) (holding that a state grantee bore the burden of "ensuring that its accounting system provide[d] adequate information"); *New City Health Ctr.* at 10 (holding that "two computer crashes [that] destroyed" records did not excuse the grantee from its obligation to "maintain proper documentation to support its use of federal funds").

Because MDLC has not demonstrated that \$410.48 in NDRN membership fees were allocable to its PAIMI grant, we affirm the disallowance of those costs.

- 2. *Water cooler rental* (\$268.75)
- Coffee services* (\$518.78)
- Audit and accounting* (\$1,493.09)
- Office moving* (\$896.69)
- Video camera* (\$55.97)
- Miscellaneous "supermarket" items* (\$113.74)
- Printing* (\$477.63)

MDLC charged its PAIMI grants for portions of its expenditures on water cooler rental⁵; coffee services⁶; audit and accounting services⁷; office moving⁸; purchase of a video

⁵ SAMHSA Ex. A, items 254-303 (FYs 2009-2010)

⁶ SAMHSA Ex. A, items 304-369, 372-76, 381-400, 402-416, 425-434 (FYs 2008-2010)

⁷ SAMHSA Ex. A, items 156-59 (FYs 2008, 2010, and 2011)

⁸ SAMHSA Ex. A, items 172-73 (FY 2008)

camera⁹; miscellaneous “supermarket” items¹⁰; and printing.¹¹ SAMHSA disallowed the costs for the same reason it disallowed the NDRN membership fees – insufficient documentation of how MDLC determined the PAIMI program’s share of its expenditures on these items and services. The documentation was in fact inadequate: MDLC provided no cost accounting reports or other contemporaneous financial records documenting its cost allocation methodology and calculations. And for all but one item (the video camera, MDLC Ex. 237), MDLC failed to submit documentation that an expense was actually incurred. Without the documentation just described, we cannot verify that MDLC charged its PAIMI grants in accordance with “relative benefits received,” a basic condition for allowability under federal cost principles. Accordingly, we affirm the disallowance of the costs specified in the heading of this section.

3. *Cleaning services performed by employee* (\$18.55)

In 2010, MDLC paid a “one-time-only stipend” of \$150 to an MDLC employee for office cleaning services performed outside regular work hours. *See* MDLC Ex. AA (items 239-42); Reply at 12. MDLC charged \$18.55 of that expense to the PAIMI program, a charge that SAMHSA disallowed. *See* SAMHSA Ex. A (items 237-38); Reply at 12. MDLC asserts that, during the audit process, it “provided SAMHSA a detailed explanation of the expenditure and an explanation as to why it was more advantageous for MDLC to utilize the individual’s services rather than search for an outside contractor.” Reply at 12. However, MDLC did not furnish that “detailed explanation” to the Board, nor did MDLC submit other evidence that the stipend was “reasonable for the performance of [its PAIMI] award[.]” 2 C.F.R. Part 230, App. A, ¶ A.2.a (Jan. 1, 2012). Even if the stipend met that condition, the portion of that expense charged to the PAIMI program is unallowable because MDLC failed to produce documentation verifying that the amount was allocable to the program – that is, charged to the program in accordance with the relative benefits received. For all these reasons, we affirm the disallowance of the cleaning services cost.

4. *Professional services* (\$4,027.44)

SAMHSA disallowed costs totaling \$4,027.44 for various “professional services.” That figure reflects seven discrete transactions, identified as items 146 through 152 on SAMHSA’s spreadsheet of questioned costs. *See* SAMHSA Ex. A. Addressing each transaction separately, we conclude that MDLC has failed to document the allowability of any of the professional services costs.

⁹ SAMHSA Ex. A, items 237-38 (FY 2008)

¹⁰ SAMHSA Ex. A, items 204-208, 224-231 (FYs 2008 and 2009)

¹¹ SAMHSA Ex. A, items 201-203 (FYs 2009 and 2010)

a. Item 146 (\$213.40)

MDLC paid \$213.40 to an individual it purportedly hired to “assist in trial prep” during August 2008. *See* MDLC Ex. 146, at 1, 4. MDLC submitted no time sheet, invoice, or other documentation of the hours actually worked, or the nature of the work performed, by that individual. Nor did MDLC proffer evidence that its payment was fully allocable to the PAIMI program. MDLC therefore failed to establish that the cost was reasonable or allocable to its PAIMI grant, as federal cost principles require. 2 C.F.R. Part 230, App. A, ¶ A.2.a, A.2.e, A.3 (Jan. 1, 2012).

b. Item 147 (\$334.25)

On or about September 30, 2008, MDLC reportedly paid \$4,930 for “network services” provided by Network Business Solutions, Inc. *See* SAMHSA Ex. A (item 147); MDLC Ex. AA (item 147). MDLC advised SAMHSA during the audit that it had allocated \$334.25 of that expense to its PAIMI grant. MDLC Ex. AA (item 147). However, during the audit and this appeal, MDLC failed to produce accounting or other financial records showing how it determined the PAIMI grant’s share of the total expense. In addition, MDLC failed to submit for the appeal record evidence of its payment(s) for the services in question. Without such documentation, we cannot verify the allowability of any portion of the September 30, 2008 expenditure for network services.

c. Item 148 (\$442.37)

On or about October 30, 2008, MDLC allegedly paid \$11,953.73 for “network services” provided by Network Business Solutions, Inc. *See* SAMHSA Ex. A (item 148); MDLC Ex. AA (item 148). MDLC advised SAMHSA during the audit that it had allocated \$442.37 of that expense to its PAIMI grant. *See* MDLC Ex. AA (item 148). However, during the audit and this appeal, MDLC failed to produce accounting or other financial records showing how it determined the PAIMI grant’s share of the total expense. In addition, MDLC failed to submit for the appeal record evidence of its payment(s) for the services in question. Without such documentation, we cannot verify the allowability of any portion of the October 30, 2008 expenditure for network services.

d. Item 149 (\$100)

SAMHSA disallowed a \$100 payment, dated May 15, 2009, to an individual who performed “video editing.” MDLC Ex. A (item 149). MDLC produced some documentation of that cost, including a cancelled check, check stub, vendor invoice, and “Pre-Purchase Approval Form.” *See* MDLC Ex. 149. While that documentation confirms that MDLC actually made the payment, it does not describe the content of the

video that was edited or the video's relationship to MDLC's protection-and-advocacy work; the "Pre-Purchase Approval Form" indicates only the video-editor's services related to "education" and an unspecified "rights" project. In addition, MDLC does not justify its allocation of the entire \$100 expense to the PAIMI program. In short, MDLC did not adequately document the allowability of that expense.

e. Item 150 (\$621.07)

On or about July 31, 2010, MDLC reportedly paid \$6,124.97 for information technology (IT) services. *See* SAMHSA Ex. A (item 150). MDLC advised SAMHSA during the audit that it had allocated \$621.07 of that expense to its PAIMI grant. MDLC Ex. AA (item 150). However, during the audit and this appeal, MDLC failed to produce accounting or other financial records showing how it determined the PAIMI grant's share of the total expense. MDLC also failed to submit for the appeal record evidence of its payment(s) for the services in question. Without such documentation, we cannot verify the allowability of any portion of the July 31, 2010 expense for IT services.

f. Item 151 (\$1,500)

The next disputed cost relates to a 2011 "Consulting Agreement" between MDLC and the Justice Policy Institute (JPI). *See* SAMHSA Ex. A (item 151); MDLC Ex. AA (item 151); MDLC Ex. 151. The agreement called upon JPI to work with MDLC to "create a policy brief around the issue of people in Maryland who are being held at secure mental health institutions because they have been declared incompetent to stand trial" on criminal charges, and to "work with MDLC to disseminate the [policy] brief broadly to the media, policymakers and advocates."¹² MDLC Ex. 151 (MDLC-JPI Agreement, App. A). The agreement included a schedule of payments by MDLC to JPI, with the initial payment of \$3,000 due "[u]pon receipt of signed contract." *Id.* (MDLC-JPI Agreement, App. B).

¹² The agreement's scope-of-work further stated that the policy brief "will outline the problem at hand and include information around the types of offenses for which people were charged, the length of time they have been committed, the types of services and treatment plans that the court is requiring in order for someone to be released to the community, the extent to which prosecutors are extending the period of commitment through refilings, and policy recommendations." MDLC Ex. 151 (MDLC-JPI Agreement, App. A).

MDLC made the initial payment on or about June 9, 2011 and charged one-half of that expense to the PAIMI grant and the other half to a grant issued under the Traumatic Brain Injury (TBI) State Partnership Grant Program (a program administered by HHS's Administration for Community Living). The Consulting Agreement resulted in the issuance of an October 2011 report by JBI titled, "When Treatment is Punishment: The Effects of Maryland's Incompetency to Stand Trial Policies and Practices" (JPI Report).¹³

MDLC asserts that the JPI report is "directly related to the goals of the PAIMI program." MDLC Ex. AA (item 151). But MDLC does not further explain the relationship except to say that "individuals with mental illness" include those who may be eligible for grant-funded protection-and-advocacy services may include persons who have been "adjudicated incompetent to stand trial and held in Maryland's state psychiatric hospitals." See Reply at 6. A PAIMI program grantee must establish annual "priorities" that specify "goals" and "objectives" to "implement the established priorities." 42 C.F.R. §§ 51.22(a), 51.24(a). MDLC does not indicate which of its established annual priorities was advanced by the consulting agreement with JPI. Nor does it explain how the JPI report's findings helped it carry out the legal "protection and advocacy services" funded by its PAIMI grant. MDLC asserts that one need only "glance through the [JPI Report] to determine that [the project] related to the PAIMI program," Reply at 6, but the report does not discuss MDLC's role or involvement, if any, in competency evaluations and determinations (for criminal justice purposes); identify problems with, or recommend improvements to, Maryland's protection and advocacy system; or discuss how MDLC's work is affected by the State of Maryland's competency determination practices. In short, MDLC has not carried its burden of connecting the JPI report to specific grant purposes or establishing that its report-related costs were "reasonable for the performance of" its PAIMI grant. 2 C.F.R. Part 230, App. A, ¶ A.2.a (Jan. 1, 2012). Even if the report benefited the PAIMI program, the contract costs are unallowable because MDLC does not specify the basis for its decision to allocate one-half of the initial contract payment to the PAIMI grant and the other half to the TBI grant, or explain why those two federal awards were the only funding sources or organizational cost objectives which benefited from the work performed by JPI.

g. Item 152 (\$816.35)

On or about October 31, 2011, MDLC allegedly paid \$6,345.00 for IT services provided by Network Business Solutions, Inc. See SAMHSA Ex. A (item 152); MDLC Ex. AA (item 152). MDLC advised SAMHSA during the audit that it allocated \$816.35 of that expense to its PAIMI grant. MDLC Ex. AA (item 152). However, during the audit and

¹³ The report is available at http://www.justicepolicy.org/uploads/justicepolicy/documents/when_treatment_is_punishment-full_report.pdf (last visited Jan. 5, 2018).

this appeal, MDLC failed to produce accounting or other financial records showing how it determined the PAIMI grant's share of the total expense. MDLC also failed to submit for the appeal record evidence of its payment(s) for the services in question. Without such documentation, we cannot verify the allowability of any portion of the October 31, 2011 expense for IT services.

5. *Employee travel* (\$2,392.63)

SAMHSA disallowed travel costs totaling \$2,392.63. That figure reflects the transactions identified as items 127, 131-140, 142, and 143 on SAMHSA's spreadsheet of questioned costs. *See* SAMHSA Ex. A. We discuss each transaction (or group of related transactions) separately.

a. Item 127 (\$123.68)

MDLC charged \$123.68 to its PAIMI grant for an employee's "mileage." *See* SAMHSA Ex. A (item 127). In support of the charge, MDLC submitted three pieces of documentation: a cancelled check for \$123.68 made out to the employee; a timesheet; and a travel expense voucher signed by the employee's supervisor. MDLC Exs. 127-28. The voucher indicates that, on nine days between June 11 and June 27, 2008, the employee traveled 255 miles "From/To" "Spring Grove," "Springfield," or "Sheppard Pratt" and that the reimbursement due for that mileage was \$123.68 (or 255 miles multiplied by the mileage rate of 0.485 per mile). MDLC Ex. 128. SAMHSA contends that Petitioner's documentation is inadequate because it does not "articulat[e] the purpose of the travel and its relationship to the PAIMI grants." Supplementary Respondent's Brief at 3. However, the destinations noted on the expense voucher – Spring Grove, Springfield, and Sheppard Pratt – are Maryland psychiatric institutions. *See* <http://msa.maryland.gov/msa/mdmanual/16dhmh/mha/html/mhaf.html> (last visited Jan. 5, 2018) (identifying Spring Grove and Springfield as state psychiatric hospitals); <https://www.sheppardpratt.org/about> (last visited Jan. 5, 2018) (identifying Sheppard Pratt as a Maryland non-profit mental health provider). That information is sufficient evidence that the purpose of the employee's trip was to interact with persons eligible (or potentially eligible) for protection-and-advocacy services or with those persons' caregivers – an essential PAIMI program function. *See* 42 C.F.R. § 51.31(c) and (d) (stating that "[w]herever possible, the [PAIMI] program should establish an ongoing presence in residential mental health care or treatment facilities, and relevant hospital units," and that "[p]rogram activities should be carried out in a manner which allows program staff to . . . [i]nteract regularly with those individuals who are current or potential recipients of protection and advocacy services" and "[i]nteract regularly with staff providing care or treatment"); *Delta Health Alliance*, DAB No. 2624, at 15-16 (2015) (allowing mileage costs based on an expense reimbursement form showing that travel was for official purposes). **We therefore reverse the disallowance of these mileage costs.**

b. Items 131-140 (\$266.95)

MDLC paid \$1,652.84 to enable its executive director (Virginia Knowlton) to attend: (1) a two-day “New Executive Director Training” program in Phoenix, Arizona on May 11 and 12, 2010; and (2) a June 2010 NDRN conference in Orlando, Florida. *See* SAMHSA Ex. A (items 131-140); MDLC Ex. 131 (payment and other records); MDLC Ex. 132 (Phoenix training agenda). MDLC charged \$266.95 of that amount to its PAIMI grant. SAMHSA Ex. A (items 131-140 (“Amount Reviewed” column)).

SAMHSA found that the executive director’s attendance at the Phoenix conference did not benefit the PAIMI program. SAMHSA Ex. A (item 131 (column for “OFAS Comments”)). MDLC does not rebut that specific finding. It says only that it “provided sufficient documentation to illustrate” that costs incurred to attend the conference were allowable costs of its PAIMI grant. Reply at 5. But aside from documentation of travel logistics, the only evidence submitted by MDLC concerning the Phoenix conference is its two-page meeting agenda. MDLC Ex. 132. MDLC does not point to any aspect of that agenda to support its implicit claim that the executive director’s attendance at the conference was an “ordinary and necessary” organizational expense and otherwise “reasonable” for the performance of its PAIMI award. Furthermore, MDLC failed to produce accounting or other financial records verifying that the PAIMI grant was charged no more than its allocable share of the Phoenix and Orlando trip expenses. For these reasons, we sustain the disallowance of the executive director’s travel costs.

c. Item 142 (\$341.55)

MDLC charged its PAIMI grant \$879.10 for travel expenses relating to a conference hosted by the National Association for Rights Protection & Advocacy (NARPA) in Atlanta, Georgia from September 8 through September 11, 2010. *See* SAMHSA Ex. A (item 142). SAMHSA allowed \$537.55 of those costs – for a hotel room and per diem expenses for one employee, Laura Cain – but disallowed the balance of \$341.55. *Id.* The disallowed expense is identified on a reimbursement request form as a hotel room charge for a second MDLC employee named Sarah Rhine. MDLC Ex. 142, at 2. However, Rhine’s name does not appear on a copy of any hotel bill submitted by MDLC, *see id.* at 3-4, and there is no other evidence (such as airline ticket receipt or other travel document) confirming that she attended the conference in her capacity as a MDLC employee. Furthermore, a “Pre-Purchase Approval Form” indicates that MDLC authorized the purchase of only one round-trip airline ticket and one hotel room for the conference, raising the question of whether Rhine’s attendance, assuming it occurred, was reasonable and related to MDLC’s protection-and-advocacy work. Given the inconclusive (at best) documentation before us, we hold that MDLC has not carried its burden of documenting the allowability of \$341.55 for travel to the September 2010 NARPA conference.

d. Item 143 (\$1,660.45)

MDLC charged its PAIMI grant \$1,660.45 for travel expenses (airfare, lodging, etc.) incurred by employee Laura Cain to attend a Florida film festival in September 2010. *See* SAMHSA Ex. A (item 143); MDLC Ex. 145. The ostensible purpose of the trip was to allow Cain to present a documentary film, titled “Healing Neen,” about one woman’s recovery from trauma; to discuss with film audiences and others about how the film is used to promote awareness and understanding of trauma’s impact on mental health and substance abuse disorders; and to explain how the film “fit within [MDLC’s] mission and goals and its success in expanding trauma-informed care in Maryland and beyond through its use in training.” MDLC Ex. 143, at 1-2.

SAMHSA’s reason for disallowing these travel costs relates to the film’s production, not to its subject matter or the purpose of the Florida trip. MDLC produced “Healing Neen” under a contract with the Washington County (Maryland) Mental Health Authority (WCMHA), which provided \$50,000 to cover production costs. SAMHSA Ex. A (item 143 (“OFAS Comments”)); SAMHSA Ex. K, at 2. MDLC in turn hired three companies to create the film. SAMHSA Ex. K, at 2. Laura Cain, a “managing attorney” with MDLC, was the resident agent and co-owner of one these companies (True Lens Productions, LLC, dissolved in 2009) and the owner of a second (In the Hollow Films). *See id.*; SAMHSA Ex. L. The funds used to pay for the film’s production had been awarded by SAMHSA to the Maryland Mental Hygiene Administration (and passed through to WCMHA) under the Projects for Assistance in Transition from Homelessness (PATH) program.¹⁴ SAMHSA Ex. K, at 2; SAMHSA Ex. A (item 143 (column for “OFAS Comments”)).

Section 74.42 of HHS’s grant administration regulations states:

No employee, officer, or agent [of a “recipient”¹⁵] shall participate in the selection, award, or administration of a contract supported by federal funds if a real or apparent conflict of interest would be involved. Such a conflict would arise when the employee, officer, or agent, or any member of his or her immediate family, his or her partner, or an organization which employs or is about to employ any of the parties indicated herein, has a financial or other interest in the firm selected for an award.

¹⁴ The Maryland Mental Hygiene Administration is now known as the Maryland Behavioral Health Administration, which is a part of the Maryland Department of Health. The Maryland Department of Health was formerly called the Maryland Department of Health and Mental Hygiene.

¹⁵ The term “recipient” is defined in the grant administration regulations to mean “an organization receiving financial assistance directly from an HHS awarding agency to carry out a project or program.” 45 C.F.R. § 74.2 (Oct. 1, 2012).

45 C.F.R. § 74.42 (Oct. 1, 2012). In addition, section 51.26 of the PAIMI program regulations states:

The P&A system must develop appropriate policies and procedures to avoid actual or apparent conflict of interest involving clients, employees, contractors and subcontractors, and members of the governing authority and advisory council, particularly with respect to matters affecting client services, particular contracts and subcontracts, grievance review procedures, reimbursements and expenses, and the employment or termination of staff.

42 C.F.R. § 51.26.

Based on 45 C.F.R. § 74.42, SAMHSA contends that Laura Cain's September 2010 travel costs are unallowable because Cain "participated in administering a contract supported by SAMHSA funds where a conflict of interest was involved" – the alleged conflict being Cain's financial or other interest in the two companies hired by MDLC to produce "Healing Neen." SAMHSA Br. at 16. SAMHSA further contends that the travel costs are unallowable under 42 C.F.R. § 51.26 because MDLC "did not apply its policies and procedures in such a manner as to avoid an actual or apparent conflict of interest involving Ms. Cain and her film companies with which MDLC entered into a sole source contract." *Id.*

MDLC responds that Cain's trip to discuss "Healing Neen" is "related" to the PAIMI program, emphasizing that the film "has been used to train mental health professionals regarding trauma informed care practices across the nation and internationally" and has "received awards in several film festivals[.]" App. Br. at 5. MDLC also contends that "[n]o conflict of interest was involved" in making the film, relying upon an argument made by the State of Maryland in a March 1, 2013 letter objecting to a proposed disallowance by SAMHSA of film production costs charged to the PATH program. *Id.* at 5-6; *see also* Reply at 14; SAMHSA Ex. K (March 1, 2013 letter from K. Morse (state of Maryland) to L. Stallworth (SAMHSA)).

We hold that the disallowance of Laura Cain's September 2010 travel costs cannot be sustained under either 45 C.F.R. § 74.42 or 42 C.F.R. § 51.26 because the record fails to establish that those costs stem from a conflict of interest as defined in section 74.42. Section 74.42 prohibits an officer, employee, or agent of the grantee from participating in the award or administration of a grant-supported contract when such activity involves a "conflict of interest," and further provides that such a conflict exists when that person "has a financial or other interest in the firm selected" as the grantee's contractor. SAMHSA's disallowance of the travel costs is a finding that they are "not in

compliance” with section 74.42’s prohibition of conflicts of interest in grantee contracting. *See* 45 C.F.R. § 74.62(a)(2). Hence, the issue before us is whether the disputed travel costs were incurred in connection with a grant-supported contract that was awarded or administered by an MDLC employee, officer, or agent having a financial or other interest in the selected contractor.

We see no evidence of any connection between the travel costs and a conflict-laden contract. Those costs do not constitute direct payments to a contractor hired by MDLC to perform grant-funded work. In addition, the costs were not authorized or required by any contract in which Laura Cain (or some other MDLC employee, officer, or agent) had a financial or other interest. The contract that SAMHSA identifies as being tainted by a conflict of interest – a contract funded by the PATH program – relates to the *production* of “Healing Neen,” not to MDLC’s use of the finished film for educational or advocacy purposes. Further undermining SAMHSA’s position is its failure to state a legal reason why a possible conflict of interest involving a contract funded by the PATH program can be imputed to MDLC’s use of funds awarded under the PAIMI program.¹⁶

An additional problem with SAMHSA’s position is that the record is unclear about whether MDLC violated section 74.42 in overseeing the production of “Healing Neen.” That regulation governs the conduct of employees, officers, or agents of the “recipient” – that is, the entity that receives funds directly from the HHS awarding agency. It appears that MDLC was not the “recipient,” or grantee, of the PATH funds which financed the film’s production; rather, the recipient was the Maryland agency that contracted with MDLC for the production work. Furthermore, there is no evidence that MDLC was a “subrecipient” accountable to the State of Maryland for using PATH program funds in accordance with the Part 74 requirements. *See* 45 C.F.R. § 74.2 (defining “subrecipient” to mean “the legal entity to which a subaward is made and which is accountable to the recipient for the use of the funds provided”).

There being insufficient evidence and argument to support SAMHSA’s conflict-of-interest theory, and no contention by SAMHSA that Laura Cain’s September 2010 travel costs are unallowable on other grounds, **we reverse the disallowance of those costs.**

¹⁶ While it states that Laura Cain “participated in the administration of a contract supported by SAMHSA funds” (omitting to specify the SAMHSA-administered program from which those funds came), SAMHSA does not assert that reimbursing the travel costs would violate terms and conditions of the PAIMI grant.

6. *Employee bonuses* (\$583.30)

According to SAMHSA's spreadsheet of questioned costs, MDLC paid four employees a total of \$2,000 in merit bonuses during FY 2009. *See* SAMHSA Ex. A (items 174-200); MDLC Ex. AA at 7-9 (items 174-200). MDLC advised SAMHSA during the audit that it had allocated \$583.30 of that total to its PAIMI grant for that fiscal year. MDLC Ex. AA at 7-9. However, during the audit and this appeal, MDLC failed to produce accounting or other financial records showing how it determined the PAIMI grant's share of the total paid for staff bonuses. (MDLC also failed to submit for the appeal record evidence of its payment of the bonuses.)

Not only did it fail to meet its burden on the allocability issue, MDLC failed to show that it satisfied applicable cost principles relating to employee compensation. OMB Circular A-122 provides that "incentive compensation" (to motivate cost-savings or efficient or safe performance) is "allowable to the extent that": (1) employees' "overall compensation," including incentive compensation, is "reasonable"; and (2) the incentive compensation is "paid or accrued pursuant to an agreement entered into in good faith between the organization and the employees before the services were rendered, or pursuant to an established plan followed by the organization so consistently as to imply, in effect, an agreement to make such payment." 2 C.F.R. Part 230, App. B, ¶ 8.j. (Jan. 1, 2012).

MDLC submitted no evidence that the bonus recipients' "overall compensation" was "reasonable." Nor did it prove that the bonuses were "paid or accrued pursuant to" an employment agreement or incentive compensation plan that was in force "before the services were rendered." The record contains a document titled "Merit Bonus Award Policy." SAMHSA Ex. I (Attachment 4A). However, the policy does not indicate that it was in force during FY 2009, when the disallowed bonuses were paid. Furthermore, there is no evidence that the disallowed bonuses were paid in accordance with the policy's nomination procedures and other criteria.

For these reasons, we conclude that MDLC has not carried its burden of demonstrating the allowability of the FY 2009 employee bonus payments.

7. *PAIMI Council stipends* (\$1,400)

SAMHSA disallowed \$1,400 for "stipends" paid by MDLC to advisory council members during FYs 2008-2011. These expenses are identified as items 3-5, 7-13, 32, 38, 41, 52, 53, and 88 on SAMHSA's spreadsheet of questioned costs. *See* SAMHSA Ex. A.

The PAIMI program regulations state that “allotments” (that is, PAIMI grant funds) “may be used to pay for all or a part of the expenses incurred by members of the advisory council in order to participate in [the council’s] activities.” 42 C.F.R. § 51.23(d)(1). Those “[e]xpenses may include transportation costs, parking, meals, hotel costs, per diem expenses, *stipends or subsistence allowances*, and the cost of day care or child care (or its equivalent for the child’s travel and subsistence expenses) for their dependents with mental illness or developmental disabilities.” *Id.* (italics added). The regulations also state that “[e]ach P&A system shall establish its own policies and procedures for reimbursement of expenses of council members, taking into account the needs of individual council members, available resources, and applicable restrictions on use of grant funds” *Id.* § 51.23(d)(2).

As evidence of its reimbursement policies and procedures for advisory council members, MDLC submitted an undated “revised” version of its “PAIMI Advisory Orientation Manual.” MDLC Ex. BB. The manual states in relevant part that each advisory council member “shall receive a quarterly stipend of \$50 *to defray costs associated with attending meetings and as a small honorarium* to recognize the valuable contribution that each member makes to the Council and to MDLC.” *Id.* at 9 (italics and emphasis added).

During the audit, SAMHSA determined that a questioned stipend was allowable if MDLC had produced documentation that: (1) the stipend was actually paid; (2) the stipend was paid for a specific calendar quarter; and (3) the council member who received the stipend attended at least one council meeting during the quarter for which the stipend was paid. *See, e.g.*, SAMHSA Ex. A (items 35, 87). With respect to stipends that it disallowed, SAMHSA asserted in its December 7, 2015 response brief that it found MDLC’s documentation “insufficient” because it did not clearly identify the council meeting for which the stipend was paid. Respondent’s Brief at 10.

In its January 19, 2016 reply, MDLC took issue with SAMHSA’s assertion that its documentation was inadequate, asserting that the records it submitted clearly show the required link between the stipends paid to council members and those members’ attendance at council meetings during quarters for which the stipends were paid, “thereby leaving SAMHSA no reason to speculate as to the purpose for the disbursements.” Reply at 4. Without addressing that point, SAMHSA took a new tack in its May 9, 2016 sur-reply, contending the disputed stipends were subject to disallowance because: (1) they were paid in part as “honoraria”; (2) an honorarium “is not an authorized expense for which PAIMI grant funds may be used”; and (3) MDLC’s documentation for each stipend “did not differentiate which portion . . . was for an honorarium and which portion was for defraying costs to attend PAIMI Council meetings” Supplementary Respondent’s Brief at 3.

SAMHSA has not told us why it waited until its sur-reply to argue that the stipends were, to some extent, unallowable “honoraria.” It also fails to reconcile that position with its pre-disallowance decisions to approve certain stipends based on sufficient documentation of payment and of the payment’s relationship to council-meeting attendance. In addition, SAMHSA does not suggest any principled way for us to decide what portion of the stipend is for “defray[ing] costs associated with attending [council] meetings” (an allowable purpose) and which portion is, as the MDLC’s orientation manual indicates, a token of appreciation for the member’s work on the council. Nor does SAMHSA argue that a quarterly payment of \$50 is a categorically unreasonable amount for defraying members’ costs of engaging in advisory council activities. Given these circumstances, we decline to render a decision based on the reasoning stated in SAMHSA’s sur-reply brief. Consistent with SAMHSA’s practice during the audit, we will allow a disallowed stipend if there is documentation that it was actually paid for a quarter in which the council member attended at least one council meeting.

a. Item 3 (\$50)

MDLC paid advisory council member K.A. \$150 on September 15, 2008. MDLC Ex. 3. MDLC conceded that \$100 of that payment was unallowable but that the balance of \$50 represented a stipend for K.A.’s attendance at a September 4, 2007 advisory council meeting and is allowable for that reason. *See* SAMHSA Ex. A (item 3 (column for “OFAS Comments”)); MDLC Ex. AA (item 3). Although meeting minutes show that K.A. attended the September 4, 2007 meeting, *see* MDLC Ex. 1, there is no evidence – such as a notation on the cancelled check, a check voucher, or payment requisition form – that the disallowed September 15, 2008 payment was a stipend for the member’s attendance at that meeting. We therefore hold that MDLC did not adequately document the allowability of the September 15, 2008 payment to K.A. and sustain the disallowance of the balance of that payment.

b. Item 4 (\$150)

On February 13, 2009, MDLC paid advisory council member D.C. \$150. MDLC Ex. 4. As evidence of that payment, MDLC submitted a cancelled check and check voucher, the latter indicating that the payment represented stipends for D.C.’s attendance at advisory council meetings during the second, third, and fourth calendar quarters of 2008. *Id.*; *see also* MDLC Ex. AA (item 4); MDLC Ex. 2. Meeting minutes show that D.C. attended council meetings during the second and fourth quarters of 2008; there is no evidence of D.C. having attended a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at meetings on January 29, April 22, June 10, October 7, and December 9). We therefore hold that **MDLC adequately documented the allowability of the disputed stipend payments (totaling \$100) to council member D.C. for the second and fourth quarters of 2008** and sustain the disallowance of the \$50 payment to D.C. for the third quarter of that year.

c. Item 5 (\$150)

MDLC paid advisory council member J.B. \$150 on February 13, 2009. MDLC Ex. 5. MDLC contends that that payment represented stipends for J.B.'s attendance at council meetings during the second, third, and fourth calendar quarters of 2008. *See* SAMHSA Ex. A (item 5 (column for "OFAS Comments")); MDLC Ex. AA (item 5). There is no evidence that J.B. attended a council meeting during the third quarter of 2008. *See* MDLC Ex. 2. And although meeting minutes confirm that J.B. attended council meetings during the second and fourth quarters of 2008, *see id.*, there is no evidence – such as a notation on the cancelled check, a check voucher, or a payment requisition form – verifying that the February 13, 2009 payment represented stipends for attending those meetings. We therefore hold that MDLC did not adequately document the allowability of the February 13, 2009 payment to J.B. and accordingly sustain the disallowance of that payment.

d. Item 7 (\$50)

MDLC paid advisory council member T.G. \$150 on February 13, 2009. MDLC Ex. 7. MDLC conceded that \$100 of that payment was unallowable but contends that the balance of \$50 was a stipend for T.G.'s attendance at a December 9, 2008 council meeting and is allowable for that reason. *See* SAMHSA Ex. A (item 7 (column for "OFAS Comments")); MDLC Ex. AA (item 7). Meeting minutes confirm that T.G. attended the December 9, 2008 meeting (during the fourth calendar quarter of 2008), *see* MDLC Ex. 2, and a check voucher indicates that the February 13, 2009 payment included a stipend for the fourth quarter of 2008, *see* MDLC Ex. 7. We therefore hold that **MDLC adequately documented the allowability of the disputed \$50 stipend payment to council member T.G. for the fourth quarter of 2008.**

e. Item 8 (\$100)

MDLC paid advisory council member S.J. \$150 on February 13, 2009. MDLC Ex. 8. MDLC conceded that \$50 of that payment was unallowable but contends that the balance of \$100 represented stipends for S.J.'s attendance at council meetings during the second and third calendar quarters of 2008 and is allowable for that reason. *See* SAMHSA Ex. A (item 8 (column for "OFAS Comments")); MDLC Ex. AA (item 8). Meeting minutes show that S.J. attended council meetings during the second quarter of 2008; there is no evidence of S.J. attending a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at meetings on April 22 and June 10). A check voucher indicates that the February 13, 2009 payment included a stipend for the second quarter of 2008. *See* MDLC Ex. 8. We therefore hold that **MDLC adequately documented the allowability of the disputed \$50 stipend paid to council member S.J. for the second quarter of 2008** and sustain the disallowance of the disputed payment (of \$50) for the third quarter of that year.

f. Item 9 (\$50)

MDLC paid advisory council member E.K. \$50 on February 13, 2009. MDLC Ex. 9. MDLC contends that that payment was a stipend for E.K.'s attendance at an October 7, 2008 council meeting. *See* SAMHSA Ex. A (item 9 (column for "OFAS Comments")); MDLC Ex. AA (item 9). Although meeting minutes confirm that E.K. attended the October 7, 2008 meeting (during the fourth calendar quarter), *see* MDLC Ex. 2, there is no documentary evidence – such as a notation on the cancelled check, a check voucher, or a payment requisition form – verifying that the February 13, 2009 payment was a stipend for attending that meeting. We therefore hold that MDLC did not adequately document the allowability of the February 13, 2009 payment to E.K. and accordingly affirm the disallowance of that payment.

g. Item 10 (\$100)

MDLC paid advisory council member R.L. \$150 on February 13, 2009. MDLC Ex. 10. MDLC conceded that \$50 of that payment was unallowable but contends that the balance of \$100 represented stipends for R.L.'s attendance at council meetings during the third and fourth calendar quarters of 2008 and is allowable for that reason. *See* SAMHSA Ex. A (item 10 (column for "OFAS Comments")); MDLC Ex. AA (item 10). Meeting minutes show that R.L. attended a fourth-quarter council meeting; there is no evidence of him attending a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at a December 9 meeting). A check voucher indicates that the February 13, 2009 payment included a stipend for the second quarter of 2008. MDLC Ex. 10. We therefore hold that **MDLC adequately documented the allowability of the \$50 stipend paid to council member R.L. for the fourth quarter of 2008** and sustain the disallowance of the disputed payment (of \$50) for the third quarter of that year.

h. Item 11 (\$150)

On February 13, 2009, MDLC paid advisory council member S.M. \$150. MDLC Ex. 11. MDLC contends that the payment represented stipends for S.M.'s attendance at council meetings during the second, third, and fourth calendar quarters of 2008. *See* MDLC Ex. AA (item 11). Meeting minutes show that S.M. attended council meetings during the second and fourth quarters of 2008; there is no evidence that she attended a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at meetings on April 22, October 7, and December 9). A check voucher indicates that the February 13, 2009 payment included stipends for the second and fourth quarters of 2008. MDLC Ex. 11. We therefore hold that **MDLC adequately documented the allowability of the stipends (totaling \$100) paid to council member S.M. for the second and fourth quarters of 2008** and sustain the disallowance of the disputed payment (of \$50) for the third quarter of that year.

i. Item 12 (\$150)

On February 13, 2009, MDLC paid advisory council member L.P. \$150. MDLC Ex. 12. MDLC contends that the payment represented stipends for L.P.'s attendance at council meetings during the second, third, and fourth calendar quarters of 2008. *See* MDLC Ex. AA (item 12). Meeting minutes show that L.P. attended council meetings during the second and fourth quarters of 2008; there is no evidence that he attended a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at meetings on June 10, October 7, and December 9). A check voucher indicates that the February 13, 2009 payment included stipends for the second and fourth quarters of 2008. MDLC Ex. 12. We therefore hold that **MDLC adequately documented the allowability of the stipends (totaling \$100) paid to council member L.P. for the second and fourth quarters of 2008** and sustain the disallowance of the disputed payment (of \$50) for the third quarter of that year.

j. Item 13 (\$150)

On February 13, 2009, MDLC paid advisory council member T.W. \$150. MDLC Ex. 13. MDLC contends that the payment represented stipends for T.W.'s attendance at council meetings during the second, third, and fourth calendar quarters of 2008. *See* MDLC Ex. AA (item 13). Meeting minutes show that T.W. attended council meetings during the second and fourth quarters of 2008; there is no evidence that he attended a third-quarter council meeting, however. *See* MDLC Ex. 2 (showing attendance at meetings on April 22, June 10, and December 9). A check voucher indicates that the February 13, 2009 payment included stipends for the second and fourth quarters of 2008. MDLC Ex. 13. We therefore hold that **MDLC adequately documented the allowability of the stipends (totaling \$100) paid to council member T.W. for the second and fourth quarters of 2008** and sustain the disallowance of the disallowance of the disputed payment (of \$50) for the third quarter of that year.

k. Item 32 (\$50)

On June 30, 2009, MDLC paid advisory council member T.G. \$50. MDLC Ex. 32. MDLC contended that the payment was a stipend for T.G.'s attendance at a council meeting during the second calendar quarter of 2009. *See* MDLC Ex. AA (item 32). Meeting minutes show that T.G. attended a council meeting during that quarter (on April 14, 2009), and a check voucher indicates that the June 30, 2009 payment was a stipend for that quarter. MDLC Exs. 6, 32. We therefore hold that **MDLC adequately documented the allowability of the \$50 stipend paid to council member T.G.** for the second quarter of 2009.

l. Item 38 (\$50)

On June 30, 2009, MDLC paid advisory council member T.W. \$50. MDLC Ex. 38. MDLC contended that the payment was a stipend for T.W.'s attendance at a council meeting during the second calendar quarter of 2009. *See* MDLC Ex. AA (item 38). Meeting minutes show that T.G. attended a council meeting during that quarter (on April 14, 2009), and a check voucher indicates that the June 30, 2009 payment was a stipend for that quarter. MDLC Exs. 6, 38. We therefore hold that **MDLC adequately documented the allowability of the \$50 stipend paid to council member T.W.** for the second quarter of 2009.

m. Item 41 (\$50)

On January 12, 2010, MDLC paid advisory council member K.A. \$100. MDLC Ex. 41. MDLC conceded that \$50 of that payment is unallowable but contends that the balance of \$50 is a stipend for K.A.'s attendance at a council meeting during the third calendar quarter of 2009 and is allowable for that reason. *See* SAMHSA Ex. A (item 41 (column for "OFAS Comments")); MDLC Ex. AA (item 41). Meeting minutes show that T.G. attended a council meeting during the third quarter of 2009 (on September 8, 2009), and a check voucher indicates that the January 12, 2010 payment was a stipend for that quarter. MDLC Exs. 14, 41. We therefore hold that **MDLC adequately documented the allowability of the disputed \$50 stipend payment to council member K.A. for the third quarter of 2009.**

n. Item 52 (\$50)

Item 52 on SAMHSA's spreadsheet of questioned costs refers to an April 15, 2010 payment of \$50 to advisory council member L.G. for her attendance at a March 2010 council meeting. SAMHSA Ex. A (item 52). SAMHSA disallowed that payment on the ground that it was a second – or "duplicate" – payment for a March 2, 2010 council meeting, with the first payment identified as item 48 on the spreadsheet. SAMHSA Ex. A (item 52 (column for "OFAS Comments")). However, item 52 appears to describe the *same* payment as the one in item 48 (the latter which SAMHSA allowed). *Compare* Item 48 of SAMHSA Ex. A (referencing check no. 30986) and Item 52 (referencing check no. 30986). Consequently, it appears that MDLC did not make *two stipend payments* to L.G. for the March 2010 council meeting. Rather, it appears only that there are *duplicate entries* on SAMHSA's spreadsheet for a payment that SAMHSA determined to be allowable. Accordingly, **we reduce the disallowance by \$50** to account for that duplication.

o. Item 53 (\$50)

On April 14, 2010, MDLC paid advisory council member T.G. \$50. MDLC Ex. 53. MDLC alleged that this amount was a stipend for T.G.'s attendance at an advisory council meeting during the first calendar quarter of 2010. MDLC Ex. AA (item 53). However, MDLC failed to submit evidence that T.G. attended a meeting during that quarter. *See* MDLC Ex. 15 (minutes of a March 2, 2010 council meeting indicating that T.G. was absent). We therefore conclude that MDLC did not adequately document the allowability of the April 14, 2010 payment of \$50 to council member T.G. and accordingly sustain the disallowance of that payment.

p. Item 88 (\$50)

On June 1, 2011, MDLC paid advisory council member L.G. \$50. MDLC Ex. 88. MDLC alleged that this payment was a stipend for L.G.'s attendance at a council meeting during the first calendar quarter of 2011. *See* MDLC Ex. AA (item 88). Although the check voucher for the June 1, 2011 payment indicates that it was for "March 2011," rather than for L.G.'s advisory-council participation throughout the first quarter of 2011, we hold that the payment is allowable because the audit findings indicate that L.G. received a *single* \$50 stipend for the first quarter of 2011, *see* SAMHSA Ex. A (item 88 (column for "OFAS Comments")), and because meeting minutes confirm that L.G. participated in at least one council meeting during that quarter (January 4, 2011), *see* MDLC Ex. 16. We therefore hold that **MDLC adequately documented the allowability of the \$50 stipend paid to council member L.G. for the first quarter of 2011.**

B. Overarching issues

In this section, we consider various overarching contentions by MDLC; none provides any basis to reduce the disallowance, however.

First, MDLC suggests that the disallowance is not founded on objective standards for judging whether cost documentation is "adequate" or sufficient. Reply at 3. We disagree. HHS's grant administration requirements, and prior Board decisions which apply them, articulate specific and objective documentation standards. At minimum, a grantee must have "accounting records" that are "supported by source documentation" (such as cancelled checks, invoices, payrolls, timesheets, and other financial and business records). 45 C.F.R. § 74.21(b)(7) (Oct. 1, 2011). Furthermore, documentation must, on its face, enable a reviewer to verify that an expenditure of federal funds meets the criteria for allowability (*e.g.*, reasonableness and allocability) specified in the cost principles. *See id.* § 74.21(b)(2) (Oct. 1, 2011) (requiring a grantee to have records that "identify

adequately” the “application of funds for HHS-sponsored activities); *Hualapai Tribal Council*, DAB No. 597, at 3-4 (1984) (stating that “an elementary principle of grants administration is the requirement that a grantee have documentation that claimed expenditures were incurred to further the purposes of the [federally supported] project”); *Action for a Better Community, Inc.*, DAB No. 2104, at 14 (2007) (stating a grantee must “prove, with *appropriate* documentation, that the [disallowed] cost is allowable under the cost principles and other relevant program requirements”). MDLC does not allege that it reasonably failed to comprehend what these principles required with respect to any of the disputed cost items.

Next, MDLC asserts that it has “sound financial management practices,” pointing to the results of independent audits of its financial statements for FYs 2013 and 2014 (SAMHSA Ex. EE).¹⁷ App. Br. at 8. Those audit findings are irrelevant, however. The issue before us is not the integrity of the MDLC’s financial statements for fiscal years 2013 and 2014, or whether MDLC has systemically adequate financial management practices, but whether specific costs charged to its PAIMI grants are allowable under the grants’ terms and conditions.

Next, MDLC contends that it “has good reason to believe that the SAMHSA auditor involved in this matter . . . has a conflict of interest due to her friendship with a disgruntled former high ranking MDLC employee that severely impair[ed] her ability to be objective in the matter.” App. Br. at 2. MDLC produced no evidence of any impropriety by the auditor or explained why the alleged conflict, assuming it existed, excused it from carrying its burden in this proceeding to demonstrate the allowability of its grant-funded costs.

MDLC further contends, with scant supporting argument, that any failure to produce relevant cost documentation should be excused because its three-year record-retention obligation under 45 C.F.R. Part 74 expired before SAMHSA asked for that documentation. *See* Reply at 8. According to MDLC, SAMHSA did not ask for cost documentation until April 2014, more than “three years beyond the end of the [most recent] fiscal year” reviewed. *Id.*

MDLC misstates the general record-retention requirement, found in 45 C.F.R. § 74.53(b) (Oct. 1, 2011). Section 74.53(b) states that “[f]inancial records, supporting documents, statistical records, and all other records pertinent to an award shall be retained for a period of *three years from the date of submission of the final expenditure report or, for*

¹⁷ MDLC also alleges unfair treatment concerning the scheduling of a June 2015 financial management review, *see* App. Br. at 8, but this allegation is likewise irrelevant to any cost-allowability issue before us.

awards that are renewed quarterly or annually, from the date of the submission of the quarterly or annual financial report” – not, as MDLC suggests, three years “from the end of the [audited] fiscal year” (italics added). (MDLC’s PAIMI grants are renewed annually, and each year’s funding may be obligated over a two-year period. See SAMHSA Ex. B.)

MDLC also overlooks 45 C.F.R. § 74.53(b)(1) (Oct. 1, 2011), which specifies the following (apparently) applicable exception to the three-year rule: “*If any litigation, claim, financial management review, or audit is started before the expiration of the 3-year period, the records shall be retained until all litigation, claims or audit findings involving the records have been resolved and final action taken.*” In other words, if the awarding agency initiates an audit of a grantee’s fiscal-year costs, and does so within the three-year period specified in section 74.53(b), then the grantee must retain cost documentation relating to those costs until any “claim, litigation or audit findings” arising from the audit, including an administrative appeal of a disallowance, are resolved.¹⁸

In this case, SAMHSA started an audit of FY 2008-2011 costs in January 2012. That event clearly falls within the three-year record-retention period applicable to FYs 2009, 2010, and 2011. Consequently, section 74.53(b) required MDLC to retain documentation of those fiscal years’ costs until any dispute arising from the audit was finally resolved.

SAMHSA’s audit may have also started within FY 2008’s three-year retention period, depending on when MDLC filed its “final expenditure report” or “annual financial report” for that year.¹⁹ MDLC offered no evidence of when it filed the applicable report, however. Even if SAMHSA started the audit after FY 2008’s retention period, that circumstance would not necessarily bar the disallowance of that year’s costs. The Board has held that a grantee is excused from documenting a cost only if it shows that relevant documentation “actually existed,” was “retained for the requisite period,” and was then “innocently destroyed.” *Pa. Dep’t of Public Welfare*, DAB No. 2631, at 14 (2015) (citing *Ca. Dep’t of Health Servs.*, DAB No. 1240, at 14 (1991)); see also *Ky. Cabinet for*

¹⁸ MDLC also fails to discuss the possible relevance of 45 C.F.R. § 74.53(g)(2) (Oct. 1, 2011), which requires grantees to maintain records of its cost allocation “proposal, plan, or other computation and its supporting records” for three years starting “at the end of the fiscal year (or other accounting period) covered by the proposal, plan, or other computation.”

¹⁹ As noted, the audit exception to the three-year retention rule is applicable if an audit is “started before the expiration of the 3-year period” (45 C.F.R. § 74.53(b)(1)) – that is, started within three years “from the date of submission of the final expenditure report or, for awards that are renewed . . . annually, from the date of the submission of the . . . annual financial report” (*id.* § 74.53(b)). If MDLC’s final expenditure or annual financial report for FY 2008 was filed after January 2009, then SAMHSA’s audit, which began in January 2012, will have started “before the expiration of the 3-year [retention] period” applicable to FY 2008.

Human Resources, DAB No. 957, at 6 (1988) (stating that “[w]hile the recovery of unallowable costs is not precluded merely on the ground that records supporting those costs were destroyed in accordance with records retention requirements, the Board will take into account the prejudice a grantee can prove which is attributable to the . . . innocent loss or destruction (of records) after expiration of the record retention period” (internal quotation marks omitted)); *Ca. Dep’t of Health Servs.*, DAB No. 1007, at 8 (1989) (rejecting a claim that the awarding agency’s disallowance was “untimely” because the State failed to show, among other things, that relevant documentation was “innocently destroyed” after expiration of the record retention period). MDLC does not assert that any of these conditions is satisfied.

Finally, MDLC contends that SAMHSA disallowed costs in bad faith, relying on pretextual or shifting, and ultimately baseless, justifications to support the disallowance. App. Br. at 4 (asserting that SAMHSA “is reaching for any excuse it can possibly find to deny legitimate program costs and is continually moving the bar in an unyielding effort to fail MDLC for clearly allowable expenses” and alleging that SAMHSA had engaged in “vindictive decision making”). MDLC further contends that SAMHSA misunderstands its “programs and business operations”; has been “inconsistent with its treatment of similar expenditures”; made an “onerous” documentation demand after delaying the matter for two years; failed to “work diligently” to resolve issues raised during the audit; and, by pursuing the audit and disallowance, has unnecessarily diverted time and other resources from MDLC’s mission. See App. Br. at 3, 9; Reply at 2-3.

As the previous section’s analyses illustrate, SAMHSA did not rely on baseless or frivolous justifications for the disallowance. MDLC’s other claims lack specificity and are unsubstantiated. Even if substantiated, those claims would not permit us to reduce or overturn the disallowance. In reviewing a disallowance, the Board is “bound by all applicable laws and regulations.” 45 C.F.R. § 16.14. Those laws and regulations authorize an awarding agency to disallow costs whose reimbursement would “materially fail[] to comply with the terms and conditions of” its award. *Id.* § 74.62(a)(2). Hence, if the grantee fails to establish that a disallowed cost materially complies with the relevant award’s terms and conditions, the Board must sustain the disallowance of that cost, irrespective of the awarding agency’s conduct in performing the underlying audit or its motives in issuing the disallowance. Cf. *AmASSI Health & Cultural Ctr.*, DAB No. 2516, at 26 (2013) (holding that the Board “must uphold an agency determination [under 45 C.F.R. Part 74] to terminate a discretionary award where termination is authorized by law and the grantee has not disproved the factual basis for the determination”); *Campesinos Unidos, Inc.*, DAB No. 2720, at 6 (2016) (noting that “the Board’s jurisdiction lies in reviewing the disallowance . . . , not in evaluating the conduct of” an audit); *Kan. Dep’t of Social & Rehab. Servs.*, DAB No. 2056, at 9 (2006) (noting, or citing decisions, that an agency’s motives in pursuing an audit or the ensuing disallowance are immaterial to

Board’s review of the disallowance). The Board has no authority to approve, on equitable grounds, the reimbursement of a cost that is charged to a grant in violation of an applicable statute or regulation. *Campesinos Unidos* at 5-6; *see also Mental Health Ass’n of Oregon*, DAB No. 2590, at 9 (2014) (Board has “no authority to waive a disallowance on the basis of equitable principles.”).

Conclusion

We reverse the disallowance of costs specified in sections A.5.a., A.5.d., A.7.b., A.7.d., A.7.e., A.7.g., A.7.h., A.7.i., A.7.j., A.7.k, A.7.l., A.7.m., A.7.n., and A.7.p. The costs allowed under those sections total \$2,584.13. We sustain the disallowance of the balance of the disputed costs, which total \$10,072.87.

_____/s/
Christopher S. Randolph

_____/s/
Constance B. Tobias

_____/s/
Susan S. Yim
Presiding Board Member